

HCIA11/2005

**IN THE HIGH COURT OF THE
HONG KONG SPECIAL ADMINISTRATIVE REGION
COURT OF FIRST INSTANCE**

INLAND REVENUE APPEAL NO.11 OF 2005

BETWEEN

LEE YEE SHING JACKY and
YEUNG YUK CHING

Appellants

and

COMMISSIONER OF INLAND REVENUE

Respondent

Before : Hon Burrell J in Court
Dates of Hearing : 20-21 March 2006
Date of Judgment : 29 March 2006

J U D G M E N T

1. This is an appeal by way of Case Stated by two taxpayers, (Mr Jacky Lee and his wife, Yeung Yuk Ching) against a decision of the Inland Revenue Board of Review (the “Board”) which dismissed the taxpayers’ appeal against the Commissioner’s determination of tax payable.

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2. The original determination is dated 3 November 2003 and relates to tax payable under personal assessments for years 1993/94 to 1997/98 inclusive. The Board heard the appeal in July 2004 and gave its decision on 6 December 2004.

3. An appeal by way of Case Stated was then commenced. Initially, there was some disagreement between the parties as to how the Case Stated should be drafted. In short, the appellants wanted it to include much of the documentation which had been before the Board. The respondent disagreed. As it turned out the dispute does not matter because the respondent's draft was later agreed. The two questions of law contained in the Case Stated are as follows:

“4. The questions of law for the opinion of the Court are:

- (i) Whether, as a matter of law, and on the facts found, it was open to conclude that personal assessments under appeal for the years of assessment 1993/94, 1994/95, 1995/96, 1996/97 and 1997/98 were not excessive or incorrect.
- (ii) Whether, as a matter of law, and on the facts found, we are entitled to reject the Taxpayers' contention that Mr Lee Yee-Shing Jacky was carrying on business and trading in his securities and future index activities within the meaning of Section 14 of the Inland Revenue Ordinance and that therefore the losses sustained by such business and trade carried on by Mr Lee during each of the years of assessment from 1993/94 to 1997/98 were properly deductible in the computation of the tax liabilities of the Appellant under Personal Assessment for the relevant years.”

4. Although the appellants had agreed that the Case Stated need not have annexed to it the bulk of the documentation that had been before the Board, a summons was nonetheless issued four working days before the hearing of this appeal asking this court to remit the case to the Board directing it to find further facts as set out in the summons. Such a remittal, if granted, would necessarily require an adjournment of the appeal.

5. After hearing submissions from Mr John J.E. Swaine for the appellants and Ms Jennifer Tsui for the respondent it transpired that the extra “findings” which Mr Swaine submitted were necessary for an intelligible hearing of the appeal could, in fact, be easily gleaned from the Board's decision and were not, in any event, controversial or disputed. Once this was established Mr Swaine agreed to withdraw the summons. The order on the summons is “Summons withdrawn with costs in the cause of the appeal”.

6. As a result the further facts upon which this appeal proceeded (in addition to the Case Stated but not in any way amending it) were:

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- (a) that the buying and selling of shares and futures undertaken by Mr Lee and Y.S. Tide Ltd (“YST”) during the years in question and which were considered by the Board did in fact take place;
- (b) that Mr Lee was the 100% owner and controller of YST; and
- (c) that YST’s trading was disclosed to the Revenue at all material times and was accepted.

7. It was also agreed that only question (ii) in the Case Stated need be addressed. The only issue before the Board and on appeal was whether Mr Lee’s purchases of shares and futures was as a trader carrying on a business. The Board decided he was not and that therefore his losses in his share transactions could not be deducted in the personal assessment. If he was a trader then his assessment was excessive, if he was not, the assessment was not excessive. Therefore the answer to question (ii) also answers question (i).

The issue

8. It is not in dispute that the onus was on the taxpayer before the Board to prove that he was carrying on a trade or business. Having failed to do so before the Board, it is also not in dispute that the onus on the taxpayer on appeal by way of Case Stated is to satisfy this court that the Board’s decision was plainly wrong and that no Board properly directed would have made the decision it did. The appeal is not a rehearing, the court does not revisit the findings of fact but the court must decide whether the Board reached the correct conclusion in law based on the facts they found. In other words, was it the right decision on the facts as they found them to be?

Background

9. Mr Lee’s employment was as a director of a number of family firms. His remuneration as a director of these firms was substantial. Throughout the 1990’s he spent much time buying and selling shares and futures. Up to 1997 his losses were greater than his gains. The majority of his transactions were in his own name but a significant number were also done through a company wholly owned and controlled by him called Y.S. Tide Ltd (YST).

10. At the beginning of 1997 he made very large profits when the stock market was surging upwards. At one point he was \$51 million in profit in 1997. Taken over the previous five years he was, at that point, \$15 million in profit. In other words his profits in the first half of 1997 exceeded all his previous losses by \$15 million.

11. However, then came the Asian financial crisis and stock exchange crash. The latter part of 1997 and 1998 left him with substantial overall losses.

12. The Commissioner taxed him on his director's remunerations and disallowed any deductions for his share transactions losses on the basis that he was not carrying on a trade or business.

The appellants' submissions

13. In a nutshell, Mr Swaine submits that question (ii) can only be answered by carefully analysing what Mr Lee actually did in relation to his buying and selling of shares. His criticism of the Board's decision is that it laid too much emphasis on peripheral matters and, as a result, failed properly to analyse Mr Lee's conduct which, if it had done, would have inevitably resulted in a conclusion that from 1992-1998 he was carrying on the business of a trader in shares.

14. He submits that the Board should have concentrated on an analysis of his volume of trading in shares, the amount of money involved, the average length of time he held shares, the number of different brokers he used, his methods of financing his purchases and so on. In particular, also, he submits that more weight should have been attached to the fact that YST did exactly the same as Mr Lee. YST was Mr Lee. So why, he asks, should they be treated differently by the Revenue?

15. Wrongly, submits Mr Swaine, the Board laid emphasis on other matters when concluding that Mr Lee's claim to have been "in business" since 1992 only arose as a result of his huge losses in late 1997 onwards. They drew incorrect inferences from the facts that Mr Lee never applied for a Business Registration Certificate until 1997/98, that he never mentioned YST to the Commissioner prior to the original determination being made but did stress its existence and dealings to the Board when seeking a review, and that he never prepared or submitted audited accounts for his "business". Moreover, they attached undue weight to their adverse findings of credibility against him and against his office assistant, Ms Suen, both of whom gave evidence before the Board.

16. In short, they found against Mr Lee because (i) they found him to be an unimpressive and less than truthful witness and (ii) he had not conducted himself during 1992-1997, in the way a man "trading" or "in business" would have done whereas, submits Mr Swaine, if they had properly analysed his day-to-day activities during those years they would, inevitably, have concluded that he had been in business of trading in shares throughout.

17. The Board, it was submitted, should have looked at all the documentation concerning his buying and selling and asked the question: Was Mr Lee consistently embarking on a profit-making scheme which was not for investment purposes? If so, he is a trader. At Mr Swaine's request and with no objection from Ms Tsui I considered some of the documentation which had been before the Board to look at Mr Lee's volume of trading, his variety of brokers, his average number of deals per day, the average length of time he held shares, his comparatively small return of dividends and so on. I looked at the same unchallenged facts that the Board looked at, not

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to alter their findings of fact but to consider whether those facts supported their conclusion in law. In the context of these facts I also revisited the argument put before the Board namely, if YST was “in business” (which the Revenue agreed it was) why wasn’t Mr Lee?

Was the Board’s decision, based on its findings, wrong in law?

18. For the reasons which follow I am satisfied that the Board’s decision was not wrong. Its primary findings of fact were either uncontentious (being based on the considerable amount of documentation before it) or unimpeachable (being facts which were perfectly properly made on the evidence before it).

19. A brief analysis of their written decision demonstrates that each step in the decision-making process was properly taken and carefully considered.

20. In its Decision the Board made the following statements, findings and conclusions. The Decision sets out:

- (1) an accurate summary of the background to the Review and the issue under consideration;
- (2) a correct outline of the law and the legal principles to be applied. Of particular note are the first two principles cited:
 - “(a) The issue as to whether a person is carrying on a trade or business is a matter of fact and degree, to be decided on all the circumstances of each case. For trading in securities or futures, there has to be a habitual and systematic course of dealing.
 - (b) The subject matter of the alleged trade or business is a factor to be considered. A private individual would rarely be considered as carrying on a business of trading in shares unless there are other associated activities. In relation to futures, by virtue of its short lifespan it would be difficult to claim that they are held as long term investment.”
- (3) a comprehensive summary of the evidence. No complaint is made that this contains any errors;
- (4) a fair summary of the taxpayer’s case in which 12 factors advanced in support of his case were listed as follows:
 - “1. He operated from a stand-alone office, which served as both the office of Y.S. Tide and his personal share trade business.

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2. He had a personal assistant cum secretary to help him to keep proper books of accounts.
 3. He operated a number of securities and margin accounts with several broker firms.
 4. He spent full time on his own share trading activities and those of the family companies during the relevant times.
 5. He did a lot of preparation work and study, discussed with dealing directors, read news on listed companies and also used the stock market channel to track his stock portfolio.
 6. He had direct telephone lines to dealer rooms of two securities firms.
 7. He was a majority owner of a securities broking firm during 1997 and 1998 and participated in the management decisions of the firm at that time.
 8. He had the necessary equipments to assist him in his business.
 9. He attended courses to learn new skills and improve old ones.
 10. His transactions were frequent, large in amount and lots. The total amount of his transactions for each year was very large.
 11. He monitored his share portfolio closely.
 12. He participated in index futures trading, sub-sub-underwriting of share offers, and short-selling.”
- (5) a similar summary of the Revenue’ s case;
- (6) its reasons (at paragraphs 29-40), a summary of which is as follows:
- (i) whether a person is carrying on a trade or business is a matter of fact and degree;
 - (ii) all the 12 factors in paragraph 27 (on pages 8 and 9 of this judgment) have been considered;

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- (iii) the onus of proof on the taxpayer has not been discharged;
- (iv) Mr Lee was “not a very truthful witness”. He was evasive and changed his evidence. He denied the fact that his family only “bailed him out” of his losses on the condition that he gave up his share dealings;
- (v) Ms Suen, his assistant, was “not an honest witness”. She was not employed by YST but by one of Mr Lee’s family businesses;
- (vi) Mr Lee’s explanation as to why YST was never mentioned to the Commissioner at the material time was unsatisfactory;
- (vii) Mr Lee’s explanation as to why he only took out a Business Registration Certificate very late in the day was unconvincing. In truth it was an “after thought” because of his losses in 1997 and 1998;
- (viii) Mr Lee failed to produce any audited accounts for his alleged business (the Board further noted that if, as claimed by Mr Lee, this was on his former accountant’s advice, the advice was good because it was not a business and there was no requirement to produce accounts);
- (ix) if he was running a business he would have used YST for all the transactions;
- (x) Mr Lee only raised the existence of YST with the Revenue when it suited him to do so as part of his argument that he was in business; namely after his major losses had been incurred and the figures accepted by the Revenue; and
- (xi) “each and every factor urged upon us by the taxpayer’s tax representative” has been “carefully considered”. The Board was “not impressed” by Mr Lee’s strategy. It “lacked professionalism” and was “unconventional to a true trader”.
- (xii) Mr Lee’s conduct in his research into and preparation for his transactions were “not uncommon to and no more than those carried out by some keen and sophisticated investors of his day”.

21. The cumulative effect of these findings makes it untenable for Mr Swaine to complain that the Board failed to analyse or properly consider what Mr Lee actually did. Equally, I find there to be no substance in the argument that no tribunal, properly directed, could have concluded that Mr Lee was not in the business of a trader in securities and futures.

The respondent's case on appeal

22. Further to and enlarging upon the matters already canvassed, Ms Tsui, on the respondent's behalf, makes the following additional points which, I agree, add weight to the respondent's submissions as to the correct answer to the question of law in the Case Stated.

(a) The issue before the Board was simply whether Mr Lee had satisfied the board members that he had been carrying on a business or trade. The question was, trade or no trade? Once answered in the negative on the facts, it was not incumbent on them to go on and define or analyse what he was doing. Once they decided that he was not trading that was the end of the matter.

(b) This court's approach to that decision is as stated in *Kwong Mile Services Ltd v. CIR* [2004] 3 HKLRD at page 178:

“... (i) in an appeal on law only the appellate court cannot substitute its own preferred inference for that drawn by the fact-finding tribunal if the primary facts justify alternative inferences of fact, but that (ii) the appellate court can and should interfere with an inference of fact drawn by the fact-finding tribunal which cannot be justified by the primary facts. In *Lim Foo Yong Sdn Bhd v Comptroller-General of Inland Revenue* [1986] STC 255, Lord Oliver said (at p.259) that ‘it is not for an appellate tribunal to substitute for the findings of the Special Commissioners what it thinks it would have found had it been hearing the original appeal but to see whether there was before the commissioners evidence on which they could properly and reasonably reach the conclusion that they did reach and whether, having regard to the facts found, their conclusions were consistent and intelligible.’”

(c) Mr Swaine's submissions concerning the operation of YST ignores the basic truth that a company and an individual are very different. YST had a Business Registration Certificate from its inception, it always declared itself to be trading and there could be no issue about its intention to do so. As stated by the Board when reciting the legal principles (*supra*) “a private individual would rarely be considered as carrying on a business unless ...”. A private individual is presumed, at the outset, not to be carrying on a business. It is then up to him to demonstrate otherwise. To apply the test — “did he embark on a profit-making scheme avoiding long term investments?” is too simplistic.

(d) The Board was fully aware of all the actual transactions made and concluded that the Commissioner's analysis of them was a proper one. The Commissioner's determination was a lengthy document which was awash with

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statistics. In particular (by way of an example in support of the conclusion that he was an enthusiastic investor rather than a true trader) it stated that, taking each sale as one transaction, between 1993 and 1998 Mr Lee's number of share transactions per day ranged from 0.43 per day to 2.67 per day. The average duration for which a share transaction was held was from 42 days to 95 days in each of those years.

- (e) The Board did not attach undue weight to their findings as to credibility. Rather, their findings on credibility were weighed properly in the overall balance.

Conclusion

23. For all the above reasons, the answer to question (ii) in the Case Stated is "yes".

24. At the conclusion of the hearing, both counsel agreed that costs should follow the event. I therefore make a final costs order that the costs of the Case Stated be paid by the appellants to be taxed if not agreed.

(M.P. Burrell)
Judge of the Court of First Instance,
High Court

Mr John J.E. Swaine, instructed by Messrs Raymond C.P. Lo & Co., for the Appellants

Ms Jennifer Tsui, instructed by Department of Justice, for the Respondent